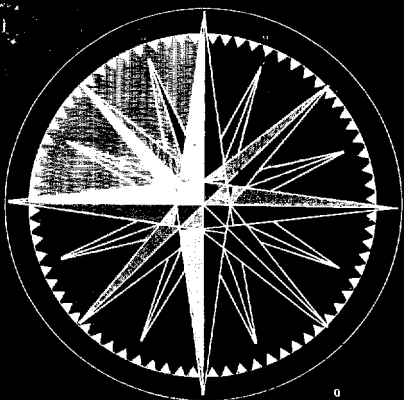


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SPECIAL REPORT

OFFICE OF CURRENT INTELLIGENCE

ECONOMIC DETERIORATION AND LEFTIST GAINS IN BRAZIL

CENTRAL INTELLIGENCE AGENCY

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3 May 1963

ECONOMIC DETERIORATION AND LEFTIST GAINS IN BRAZIL

Despite US aid and its own efforts to put its house in order, Brazil has formidable financial and economic problems. The crisis eases the extension of Communist gains, which recently have been substantial in national labor union organizations and in the Pernambuco state administration. These trends have caused increasing restlessness among the military, who are weighing the chances of bringing off a coup against President Goulart.

Financial Situation

Brazil's foreign exchange position has been deteriorating rapidly despite a reduction of imports and virtual cessation of profit remittances. Commercial arrears totaled \$138.2 million on 1 April, including arrears to petroleum companies of some \$37 million. Payment of a further debt to petroleum companies of \$17.7 million accumulated in 1962 has been postponed to September 1963. On 24 April Brazil received \$84 million in US aid as a result of recent financial negotiations in Washington. This alleviates the critical foreign exchange situation but does not resolve Brazil's problem.

The cost of living in Rio de Janeiro went up 16 percent in the first three months of 1963, rising 9.7 percent in March alone. The recent March rise probably gained impetus from the government's large currency issuances last December, which are now having peak effect in the banking system, and from the removal of subsidies in January. Government tightening of credit is expected to have

an early favorable effect on the cost-of-living rise, but it is causing dislocations in the manufacturing sector--notably in the motor vehicle industry where sales are down 50 percent and procurement of parts down 70 percent.

Communist Gains

In recent months the Communists--aided by the economic crisis--have made notable progress in labor organizations and in the administration of Pernambuco State. They now direct three of Brazil's five national labor confederations--including the National Confederation of Industrial Workers, the largest and most powerful--and have a fair chance of taking over the other two confederations this year. The Brazilian labor minister is said to be pressing for the establishment of the pro-Communist General Workers Command as a directing organ for all Brazilian labor. This step would give the Communists increased influence not only over urban labor, but also over

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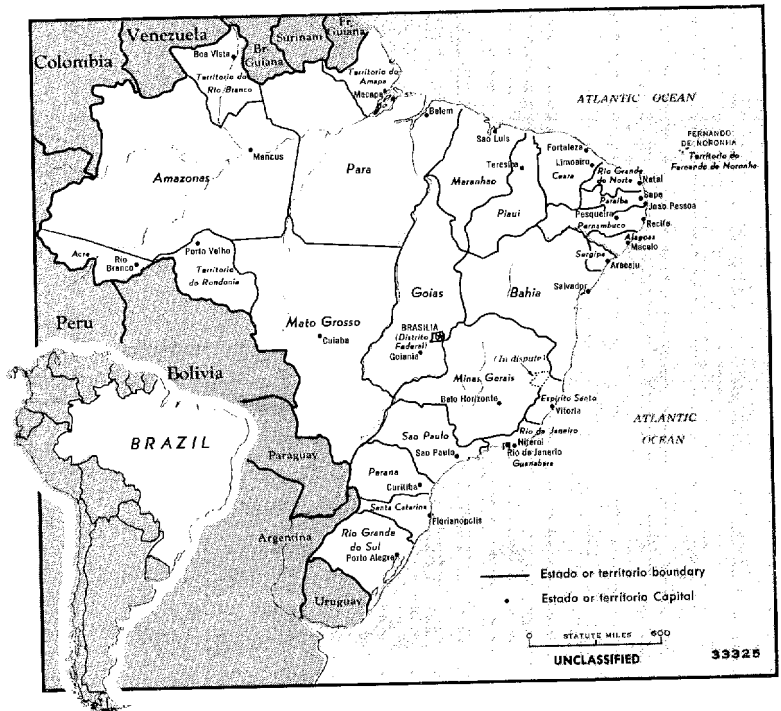
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rural labor, which now is beginning to organize.

In Pernambuco State, pro-Communist Governor Miguel Arraes has appointed Communists and extreme leftists to key positions in his administration. Although it might have been expected that Arraes would be sobered by executive responsibility, he is in fact depending more on Communists at present than he did in his previous position as mayor of Recife, the Pernambuco capital.

Particularly significant among Arraes' appointments is that of Diogenes Arruda Camara, who directed the Brazilian Communist Party during the late 1940s and early 1950s when Secretary General Prestes was in hiding. Arruda Camara has fallen from favor in the party because of his advocacy of a hard line, in contrast to the party's pro-Khrushchev position, but he is still one of the party's most important members. He is apparently in charge of Pernambuco's agrarian reform program.

Arraes' new police chief is Humberto Andrade, for years a faithful ally of the Communist Party, and possibly a member of the clandestine Communist apparatus among the military.



Unrest Among the Military

Increased Communist and pro-Communist influence in the Brazilian Government and particularly in organized labor has heightened tension in the Brazilian military. Both Goulart and the military are aware that a government with strong backing from organized labor would stand a good chance of resisting military pressure for many years, as did Juan Peron in Argentina.

The military are also seriously concerned about Goulart's promotion policies. They realize that in time he could go

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far toward neutralizing his opposition in the armed forces through further selective promotions and reassignments. They also realize that their careers will be adversely affected, at least in the short run, if they become closely associated with anti-Goulart activity.

At present, a majority of military officers are anti-Goulart, but pro-Goulart officers occupy a considerable number of key positions. In the powerful First Army, near Rio de Janeiro, pro-Goulart officers now hold the post of army commander, the three key division commands, and some subsidiary positions. Goulart has fewer adherents in the Second and Third Armies, and is weak in the small Fourth Army. This unit, however, is stationed in Pernambuco, far from Brazil's center of power.

The main efforts to organize military opposition to Goulart in recent months have revolved around several high-ranking officers, including retired Marshal Denys, and have evoked the name of former President Dutra. Denys recently stated that he hoped to have the support of key state governors and planned to give a civilian complexion to a post-revolutionary government.

Military plotting does not now appear to have reached an advanced stage, but it is continuing. Denys has endorsed the view prevalent among much of the military that a coup would be justifiable only if Goulart were to commit some flagrantly unconstitutional act, but other plotters state that such a pretext will not be necessary.

General Amaury Kruehl, Goulart's war minister, who has frequently made anti-Communist pronouncements but has taken little anti-Communist action, may hold the balance in the situation. An influential but ambiguous figure, he has reassured elements fearful of the government's leftist orientation that he is a bulwark against Communist subversion. At the same time, however, he has convinced Goulart and his labor allies that he is on their side.

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but would oppose any abrupt swerve toward the Soviet bloc. Anti-Goulart elements are seeking to persuade Kruel to join them but have thus far had no perceptible success.

Foreign Policy

The Goulart government's handling of its recent agreement with the US reflects its "independent" foreign policy, which is designed to demonstrate an ability to take positions opposing or at least differing from those of the United States. Brazil has recently encountered difficulties, however, in expressing its independence by the establishment of closer relationships with other great powers.

Brazil has been especially anxious to make closer contact with De Gaulle, whose foreign policy it considers "truly independent." However, this aspiration has been frustrated by Brazil's recent dispute with France over fisheries.

Brazil's efforts to gain increased trade and aid from

the Soviet bloc have also apparently failed to fulfill initial expectations. Protracted negotiations with the USSR for renewal of the Brazilian-Soviet trade agreement which expired on 31 December 1962 were completed only on 20 April; such a delay could indicate that it provides less Soviet oil and wheat than the Brazilians had requested. The USSR has thus far failed to make any substantial aid commitment to Brazil, although Finance Minister Dantas is planning to go to Moscow in September in a new effort to seek aid.

Outlook

President Goulart seems likely to continue his efforts to increase his personal power, primarily by strategic reassignments and promotions within the military and by building a more powerful labor movement. Goulart will probably continue trying to use Communist and pro-Communist forces in both these efforts, although he may seek also to maintain a counterbalancing non-Communist force. (SECRET NO FOREIGN DISSEM)

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